BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 1999-006-G - ORDER NO. 1999-782

OCTOBER 29, 1999

IN RE: Annual Review of South Carolina Electric and Gas Company of Purchased Gas Adjustments and Gas Purchasing Policies.	)	ORDER √MR RULING ON PGA AND GAS PURCHASING PRACTICES

This matter comes before the Public Service Commission of South Carolina (the Commission) for the Annual Review of the Purchased Gas Adjustment (PGA) and the Gas Purchasing Policies of South Carolina Electric & Gas Company (SCE&G or the Company). In addition, pursuant to Order No. 94-1117, dated October 27, 1994, in docket No. 94-008-G, the Commission considered the collection of environmental clean-up costs for the period under review.

By letter, the Commission's Executive Director instructed the Company to publish a prepared notice concerning the Annual Review of the PGA and the Gas Purchasing Policies, one time, in a newspaper of general circulation in the area affected by the review. The Notice indicated the nature of the review and advised all interested parties of the manner and time in which to file appropriate pleadings for participation in the proceeding. The Company was instructed to directly notify all of its customers affected by the review of the PGA. The Company submitted affidavits indicating that it had complied with these instructions. A Petition to Intervene was filed by the Consumer Advocate for the State of South Carolina (the

Consumer Advocate). A hearing on the Annual Review was held on October 21, 1999, at 10:30 AM in the offices of the Commission with the Honorable William Saunders, Vice-Chairman, presiding. SCE&G was represented by Catherine D. Taylor, Esquire and Frank Mood, Esquire. The Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire. The Commission Staff was represented by F. David Butler, General Counsel.

SCE&G presented the testimony of R. Dow Bailey (direct and rebuttal), W. Keller Kissam (direct and rebuttal), Harry L. Scruggs (direct and rebuttal), and Julius A. Wright (rebuttal only). The Consumer Advocate presented the testimony of Richard Hornby. The Commission Staff presented the testimony of Norbert M. Thomas and Brent L. Sires.

R. Dow Bailey, Forecast Coordinator in the Resource Planning Department of SCE&G, testified. Bailey discussed the construction of the gas peak demand forecast. Bailey testified that the first step was to create a winter period data set which contained daily firm gas sendout and corresponding weather data. This involved adjustment of total daily gas sendout to remove usage by interruptible customers, plus the calculation of Heating Degree Days (HDD) to match the gas dispatching day. The data was further divided into small firm and large firm users. Once the data bases were created, separate multiple regression models were calculated for the small and large firm customer groups to statistically relate daily sendout with weather and other explanatory variables. Individual multiple regression models were created for each firm rate group which related average daily use to daily weather and seasonal variables. Combining the disaggregated models, customer projections, furnace efficiency reductions, and weather conditions then resulted in a projected winter 1999-2000 peak demand of 326,335 MCF.

W. Keller Kissam, Vice President of Gas Operations for the Company also testified. Kissam testified as to the natural gas purchasing policies of SCE&G and the importance of the Industrial Sales Program (ISP). Kissam also offered testimony with regard to the Company's recovery of costs related to the environmental liability resulting from the cleanup of properties formerly used for manufactured gas (MGP).

Kissam noted that SCE&G contracts with South Carolina Pipeline Corporation (SCPC) for all of its natural gas supplies. Volumes are delivered from SCPC to SCE&G at 189 metered delivery points. Through Commission approved tariffs DS-1 and DISS-1, SCE&G has contracted with SCPC for a firm contract demand of 224,270 DTS per day. Kissam states that SCE&G relies on SCPC as its natural gas merchant for several reasons: 1) SCE&G does not own a pipeline system that connects SCE&G's 189 metered delivery points in its distribution system. The SCPC system provides this connection. 2)By serving SCE&G, 14 other sale-for-resale customers, plus its own direct industrial customers, SCPC exerts significant market influence. Thus, according to Kissam, SCPC's market power is a benefit to SCE&G and its customers. 3) Operation of the SCPC system is backed by nearly fifty years of experience, and SCPC has a thoroughly knowledgeable Staff. The purchase, transportation, and exchange of physical natural gas, as well as the management of various financial vehicles, are indeed complex activities requiring a high degree of competency and the latest technology. Under current conditions, according to Kissam, duplication of such staffing and equipment to carry out such functions would not be beneficial for SCE&G's customers.

Kissam testified that the Industrial Sales Program allows the Company to compete with alternate fuels in providing service to various interruptible customers. These customers could have switched to alternate fuels had it not been for the ISP program. According to Kissam, without these competitive sales, more fixed costs would be borne by the firm customers.

Kissam noted that, in order for SCE&G to meet forecasted peak demands of 341,320 DTS a day for its firm customers in Winter 1999-2000, it is necessary for SCE&G to subscribe 266,495 DTS per day of firm contract demand from SCPC. This represents an increase of 42,225 DTS per day from the present subscription. SCPC has been notified of this requirement.

Reasons necessitating this increase, according to Kissam, are the growth in SCE&G's market, plus the retiring of one propane-air facility, and the derating of the sendout capabilities of two other propane-air facilities.

Kissam states that SCE&G's purchasing practices were prudent, because they effectively balance reliability of supply and least cost. SCE&G's reliance on SCPC as a merchant affords SCE&G's customers reduced administrative costs while increasing its market power and system reliability in an energy market that changes daily. Further, the ISP program, according to Kissam, allows SCE&G to continue to retain interruptible load and reduce costs system-wide.

The environmental collection factor was also discussed by Kissam. SCE&G seeks no change in this factor from the present level.

Harry L. Scruggs, Senior Rate and Regulatory Specialist in the Gas Rate Department of SCE&G testified as to the projected base cost of gas factor. Scruggs provided historical data for the review period September 1998 through July 1999, as well as providing computations for the projected cost of gas per therm for the future period November 1999 through October 2000.

With regard to the environmental cleanup cost factor, the Company collected a total of $2,329,246 from firm and interruptible sales customers and transportation customers. The cumulative amount amortized through July 31, 1999 is $13,455,009. The Company is seeking recovery of the remaining balance of $19,456,293. SCE&G proposed that the factor remain at $.011 per therm as currently approved by the Commission.

With regard to the cost of gas, the current cost of gas is 48.182 cents per therm, approved by this Commission in Order No. 98-835. The Company requested no change to the cost of gas last year.

Considering the cost of gas data for the historical period under review, the Company, according to Scruggs, has an actual over-collection of $120,694 as of July 31, 1999. The balance at October 31, 1999 is forecast to be an under-collection of $3,664,860, which was due to the warmer than normal weather experienced in the 1998-99 winter and the resulting shortfall of sales volumes. Firm sales volumes are very dependent on the weather, according to Scruggs.

As Scruggs states, the historic cost of gas is used as the starting point to project future gas costs. This cost is adjusted for known and measurable changes for the forecasted period November 1, 1999 through October 31, 2000. Much of the projection for the commodity cost of gas was affected by NYMEX index prices.

When all calculations are completed, SCE&G recommends a change in the cost of gas from 48.182 cents per therm to 54.334 cents per therm, an increase of 6.152 cents per therm.

Scruggs notes that the end result, as projected, would have the Company experience an over-collection of $1,653 on its gas cost as of October 31, 2000. The proposed increase in contract demand would increase the cost of gas by approximately one cent per therm.

Richard Hornby, Senior Associate with Tabors, Caramanis and Associates, testified on behalf of the Consumer Advocate. Hornby made three major recommendations. First, Hornby stated that if the Commission allows SCE&G to recover the costs of the incremental 42,225 Dt/day of capacity that it will begin acquiring in November, that approval should be limited to one year, not 5 years as proposed. Second, Hornby recommends that the Commission should require SCE&G to issue, under the supervision of an expert independent third party, a Request for Proposals (RFP) for up to 42,225 Dt/Day of peaking capacity, in the form of either supply or rights to curtail deliveries, for the period November 2000 through October 2004. Third, Hornby states that the Commission should require SCE&G to present, in next year's purchased gas cost recovery proceeding, a detailed analysis of the benefits and costs of offering all customers the ability to buy their own supply service from marketers and their transportation service from SCE&G.

Hornby considered at length SCE&G's gas cost recovery rates to those of SCANA Energy Marketing and other marketers in Georgia. He concluded that SCE&G's gas cost recovery rates are higher than Georgia prices, due to competition in that State. Further, Hornby states that SCE&G has a relatively expensive mix of capacity, i.e. 68% pipeline capacity and 32% propane-air capacity, and that most gas companies use less pipeline capacity in their mixes.

In addition, Hornby criticizes the proposal to obtain additional pipeline capacity from SCPC. He notes that SCE&G might find less expensive options for ensuring reliable service over the next five years.

SCE&G filed testimony to attempt to rebut Hornby's testimony. W. Keller Kissam responded to two of Hornby's major recommendations. First, Kissam notes that limiting approval of the recovery of the costs of the incremental 42,225 Dt/Day to one year would be problematic. Kissam states that SCE&G made the request with a longer term in mind in order to assure that the additional capacity would be available for its firm customers' supply needs. If the request was limited to one year, Kissam notes that SCE&G might not be able to secure enough additional capacity from SCPC to meet its customers' needs. For this reason, SCE&G requests that the additional capacity be approved for a five year period. As Kissam states, the Commission's jurisdiction and annual oversight would continue for this decision.

Kissam also addresses the suggestion that SCE&G issue a Request for Proposals (RFP) for peaking capacity under the supervision of an independent third party. According to Kissam, such a recommendation does not have merit for pipeline capacity. A replying party would purchase the gas supply at market rates just as is done now for SCE&G. Such supply would be transported over either the Transco or Southern Natural interstate pipelines, and their interstate transportation rates would be paid.

Dr. Julius A. Wright also testified for SCE&G as a rebuttal witness. Dr. Wright notes that, with regard to Hornby's third recommendation, wherein he requests that the Commission order a detailed analysis of the benefits of offering customers the ability to buy service from marketers and transportation service from SCE&G, this is inappropriate for a PGA hearing.

Dr. Wright states that if the Commission felt that such a study was necessary, that it should be considered in an entirely new docket, and all local distribution companies and other interested parties should participate.

Dr. Wright also addresses Hornby's comparison between SCE&G's rates and the rates in the deregulated Georgia market. Dr. Wright states that such a comparison between a regulated entity's rates and the deregulated entity's rates are difficult at best, because of the differing environments, differing suppliers, and other factors. Even so, Wright attempts to compare an SCE&G's average customer bill with one in Georgia. See JAW Exhibit-3, pages 3 and 4. The exhibit seems to illustrate that the SCE&G's average customer proposed annual bill will be lower, or in two cases almost identical, to the annual bill that same customer will pay in Georgia if commodity gas prices next year are similar to the October gas prices. See Wright prefiled testimony at 8.

Norbert Thomas and Brent Sires of the Commission Staff testified. Thomas summarized the Auditing Staff's findings, and stated that Staff had verified SCE&G's gas costs and Environmental Cleanup Costs for the twelve months ended August 1999. According to Thomas, SCE&G began the period with an over-collection of ($1,619,930). The under-collection for the twelve months ended August 1999, including the projected months of September and October 1999 is $5,802,903. The cumulative under-collection is $4,182,973. SCE&G's total environmental liability is $45,300,000. After deductions of $13,534,597 for amortization and collections, and $12,388,698 from insurance commitments, the outstanding balance is $19,376,705. Thomas also testified that SCE&G was correctly recovering its gas costs pursuant to its approved tariffs. See prefiled testimony and exhibits of Thomas (Hearing Exhibit 5).

Brent Sires also testified for the Commission Staff. Sires recounted the history of the gas cost recovery procedures approved by this Commission. Sires notes that a combination of historical data and projected data allows the Company to determine the appropriate base cost of gas. In the present case, the request for an increase in the proposed base cost of gas from 48.182 cents per therm to 54.334 cents per therm results in an increase of 6.152 cents per therm. Based on an annual residential usage of 600 therms, the new base cost of gas would result in an increase of $37.08 per year per residential customer. See Sires Exhibit A, Hearing Exhibit 6.

Sires notes that his observations of SCE&G's gas purchasing policies indicate that the Company receives adequate supplies of firm gas to meet its captive customers' needs. Sires reviewed the pipeline and propane-air supplies utilized by SCE&G. Sires pointed out that, based on SCPC's years of experience and expertise in pipeline operations, SCPC can adequately supply SCE&G with its present and future gas needs. Further, Sires concluded that SCE&G receives adequate supplies of firm gas to meet its captive customers' needs and is prudent with regard to its purchase of gas supplies from SCPC. Sires also noted that in light of the many changes which continue to take place which affect the securing and transportation of gas, the Company should continue its on-going program to ensure that its gas supply is consistent with its customers' needs and to ensure that supply efficiency is maintained at reasonable costs. Sires also opined that the operation of the Company's ISP program should continue, since this mechanism allows SCE&G to compete with alternate fuels.

FINDINGS AND CONCLUSIONS

Based on the evidence in the record, the Commission makes the following findings and conclusions:

1) The gas purchasing practices of SCE&G are prudent for the period under review, and SCE&G has properly recovered its gas cost pursuant to the terms and conditions of the Company's approved tariff.

The direct testimony of Company witness Kissam, and Staff witness Sires specifically support this conclusion.

Kissam notes that SCE&G purchases its gas from SCPC under tariffs approved by this Commission. By serving SCE&G and 14 other sale-for-resale customers, plus its own direct industrial customers, SCPC exerts significant market influence, and this market power may be used to benefit the acquisition of gas for SCE&G. Further, the operation of the SCPC system is backed by nearly fifty years of experience among the various members of its knowledgeable Staff. As Kissam notes, the purchase, transportation, and exchange of physical natural gas, as well as the management of various financial vehicles are indeed complex activities, requiring a high degree of competency and the latest technology. Under current conditions, duplication of such staffing and equipment to carry out such functions would not be beneficial for SCE&G's customers. (Kissam Direct at 4.) We agree, and, in fact, believe that such duplication is wasteful and costly.

Staff witness Sires testified that SCE&G's gas purchasing policies provided adequate supplies of firm gas to meet its captive customers' needs at reasonable cost, and that he expected this to be true for the present and for the future. (Sires at 4.)

We are not unmindful of the recommendations of Consumer Advocate witness Hornby, and we discuss the merits of his recommendations later on in this Order.

2) The base cost of gas shall be 54.334 cents per therm effective and beginning with the first billing cycle in November 1999.

The direct testimony of SCE&G witness Scruggs supports this conclusion. Scruggs provided historical data for the review period September 1998 through July 1999, as well as provided computations for the projected cost of gas per therm for the future period November 1999 through October 2000. After all calculations are reviewed, the conclusion is that the base cost of gas should be increased to 54.334 cents per therm. (Scruggs at 6.) We regret this increase, but it appears that there is an inescapable conclusion that this figure represents the cost of gas for the next review period that comes closest to "zeroing out" the balance in the recovery of gas cost. Failure to institute this increase at this time would likely force the Company to under-recover their cost of gas. We would note that the Company's forecasts and models are quite sophisticated, and we are convinced that these are the best predictor of what gas costs will be in the future.

3) The Company shall continue to add a factor of $0.011 per therm in the PGA for environmental clean-up costs. This was virtually uncontested, and was discussed in the

testimony of Company witness Scruggs and Commission Staff witness Thomas. (Scruggs Direct at 2-3; Thomas at 5.)

4) The current industrial sales program shall be continued. Again, this was virtually uncontested. The program was discussed in the testimony of Company witness Kissam and Staff witness Sires. (Kissam Direct at 4-6; Sires at 7-8.)

5) SCE&G's contract with South Carolina Pipeline Corporation for additional capacity of 42,225 dekatherms per day is approved for the full five year period. Company witness Kissam testified as to the growth in SCE&G's market, plus the retiring of one propane-air facility, and the derating of the sendout capabilities of two other propane-air facilities. We believe this justifies obtaining the additional capacity. Further, Kissam also noted that signing a contract for only one year as suggested by Consumer Advocate witness Hornby could mean difficulty in obtaining needed capacity later. We agree, and, therefore, we believe the full five years is justified. (Kissam Direct at 6-8; Kissam Rebuttal at 6.)

6) The Consumer Advocate's other recommendations are denied. The RFP recommendation is specifically denied, based on the rebuttal testimony of Company witness Kissam. Kissam testifies, and we believe, that the RFP proposal does not have merit for pipeline capacity, since a replying party would purchase the gas supply at market rates, just as is done now for SCE&G. Such a supply would be transported over either the Transco or Southern Natural interstate pipelines, and their interstate transportation rates would be paid.

(Kissam Rebuttal at 6-7.) The Consumer Advocate's third recommendation involving a detailed analysis of benefits and costs of offering all customers the ability to buy their supply service from marketers and their transportation service is also denied. Dr. Julius Wright, rebuttal witness for SCE&G, correctly notes that such a study is inappropriate for a PGA hearing, and we concur in this reasoning. (Wright at 9.) We also agree that such a study might be more properly addressed in an entirely new docket, with all local distribution companies and other interested parties participating. However, we decline to establish such a docket through this proceeding.

The tariffs and rate schedules shall be filed reflecting the findings herein within five (5) days of the receipt of this Order by the Company.

This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION.

Philip T. Bradley

Chairman

ATTEST:

Gary E. Walsh

Executive Director

(SEAL)